LEGISLATIVE SERVICES AGENCY

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FISCAL IMPACT STATEMENT

LS 7453
BILL NUMBER: HB 1279
NOTE PREPARED: Jan 26, 2015
BILL AMENDED:

SUBJECT: HERO Plan.

FIRST AUTHOR: Rep. Lehman
FIRST SPONSOR:
BILL STATUS: As Introduced

FUNDS AFFECTED: <u>X</u> **GENERAL**
DEDICATED
FEDERAL

IMPACT: State

<u>**Summary of Legislation:**</u> The bill establishes the Hoosier Worker Retirement Option plan (HERO Plan) to encourage Indiana residents to increase their rate of saving and to build assets for the use of participants and their survivors and beneficiaries after a participant's retirement.

The bill establishes a Plan Board (Board) with nine members: the Treasurer of State, the Auditor of State, the Director of the Office of Management and Budget, the Commissioner of the Department of Labor, and five members appointed by the Governor. It provides that the appointed Board members serve four-year terms and that the Treasurer is the Board chair.

The bill requires the Board to provide oversight for the HERO Plan, which is administered, operated, and managed by one or more investment managers, private financial institutions, or other financial and services providers selected by the Board through a competitive bidding process. The bill requires the Board to annually prepare and adopt a written statement of investment policy. It also requires the Board to submit an annual report to the Governor and the General Assembly concerning the operating and financial performance of the HERO Plan.

The bill provides that the HERO Plan be audited annually by the State Board of Accounts, and may be audited by a certified public accountant, if the Board determines it advisable.

The bill establishes a HERO Plan administrative fund to pay any administrative expenses incurred in developing, implementing, and operating the HERO Plan.

The bill requires that the HERO Plan be maintained as individual retirement accounts (IRAs) with contributions made by payroll deduction and be offered to workers who elect to enroll by employers that voluntarily choose to participate and do not offer any other kind of retirement plan.

The bill provides that the state, the Board, and participating employers are not fiduciaries for the HERO Plan and that the HERO Plan is not a debt, liability, or obligation of the state.

The bill requires the Board, before the HERO Plan takes effect, to oversee the design and dissemination to all employers eligible to participate in the HERO Plan information about the HERO Plan. It also provides that the Board maintain an Internet web site to assist employers in identifying private sector providers of available pension and retirement plans, if providers express interest in and provide the funding for the Internet web site.

Effective Date: July 1, 2015.

Explanation of State Expenditures: *HERO Plan Board:* The Board will incur costs associated with oversight of the HERO Plan, including record keeping, reporting, accounting, legal, as well as member travel and expense reimbursement. The total estimate for these costs may be small due to the Treasurer's experience (as Board chair) with providing investment services for the state.

Additionally, the Board may incur one-time start-up costs for marketing and selecting one or more HERO Plan administrators (as the HERO Plan will be administered, operated, and managed by one or more investment managers, private financial institutions, or other financial and services providers selected by the Board through a competitive bidding process).

A similar proposal in Michigan had start-up costs for marketing estimated at more than $500,000. It is possible that some or all of these start-up costs will be absorbed by the administrator(s) who is likely to pass on the start-up costs to participants in the form of administrative fees.

The bill creates an administrative fund to be used by the Board for start-up and ongoing administrative expenses. The administrative fund may consist of appropriations into the fund, money from grants, and money received from other sources (such as gifts and donations). It is possible that any expenses not covered by the administrative fund may be paid through administrative fees that are deducted directly from investment returns on individual accounts. The Board will determine with the administrator(s) the appropriate administrative fees to charge to worker accounts.

Additional Information: The HERO Plan is a retirement account program that is sponsored by the state, but is not actually administered by the state. In this case, the Board will select one or more administrators who will offer individual retirement accounts (IRAs) via participating employers to workers who do not otherwise have access to another form of retirement savings vehicle at work. Employers are to withhold deductions into the HERO Plan on their employees' behalf, but do not make contributions into employee accounts.

The state will assist in marketing the HERO Plan, which will connect employers and workers with the administrator(s). Additionally, the Board will oversee, audit, and report on the activities of the administrator(s). However, neither the state nor the Board will act as a fiduciary for the HERO Plan, and therefore neither the Board or the state are responsible or liable for the payment of any retirement benefit under the HERO Plan.

Explanation of State Revenues: The bill will likely result in an indeterminable decrease in Individual Adjusted Gross Income (AGI) revenue because of the federal income tax benefits provided for individual contributions to IRAs. If the HERO Plan is established in CY 2015, it could reduce Individual AGI collections beginning in FY 2016. Revenue collected by the Individual AGI tax is deposited in the state General Fund.

The bill allows for the HERO Plan to provide both Roth and Traditional IRAs. Both of these IRAs offer different tax advantages to workers, and the decisions of these workers in what type of IRA to choose will affect how the bill impacts state taxable income. It is likely that worker contributions to the HERO Plan will decrease their AGI, depending upon the amount of contributions made, the type of IRA owned by the worker, as well as their own personal tax situation.

LSA is unable to estimate with any certainty the total number of employers and workers who will utilize the HERO Plan. It is also difficult to determine how much the average worker will save via the HERO Plan.

Additional Information: LSA estimates that approximately 1 million workers in Indiana do not have access to an employer-sponsored retirement plan and may qualify for this program. Generally speaking, the Bureau of Labor Statistics indicates that roughly 30% of civilian workers do not have access to employer-sponsored retirement savings plans. Of those workers who are given access through their employers, roughly 78% take advantage of retirement savings plans when offered. Generally, lower income workers have less access to employer-sponsored retirement savings plans than high-income workers, and these workers, when given the opportunity to save, save at a much lower rate than their higher income counterparts (of the lowest income workers, only 41% have access to employer-sponsored plans, and of those that do, only 53% take advantage of it).

The HERO Plan is voluntary on the part of employers as well as workers. Other states that have implemented programs similar to the HERO Plan are not yet operational and therefore do not provide information on employer participation, which is key to determining worker participation.

Additionally muddying the estimation of participation in the HERO Plan is the *myRA* program. This program is the U.S. Treasury Department's version of the proposed HERO Plan, with some differences. The *myRA* program is voluntary on the part of both the employer and the worker and allows for contributions into Roth IRAs only. Contributions into the *myRA* program are backed by the U.S. Treasury Department, as the contributions are invested in a new U.S. Treasury security, which earns interest at the same variable rate as investments in the government securities fund for federal workers, which has an average annual return of 3.39% over the ten-year period from December 2003 to December 2013. The *myRA* program launched in 2014, and participation information is not yet available.

The bill does not distinguish what type of IRA (Traditional or Roth) the HERO Plan will contain, but all contributions into member IRAs will be posttax. Individuals with IRAs may contribute up to $5,500 in posttax income per year (those over age 50 may contribute up to $6,500 per year).

Traditional IRAs and Roth IRAs have different distribution and tax advantages for individuals who own them. Simply put, contributions to Traditional IRAs are tax deductible and contributions to Roth IRAs are not. However, qualified distributions from Roth IRAs are generally not taxed, while Traditional IRA distributions are.

The majority of taxpayers who have Traditional IRAs are able to deduct their entire contribution amount. As these deductions are considered "above the line" (may be taken regardless of the taxpayer's decision to itemize), this will reduce their total income tax liability.

Additionally, low- and moderate-income workers may be eligible for a federal Saver's Credit, which offsets part of the first $2,000 of contributions. The maximum Saver's Credit is $1,000 for individuals and $2,000 for married couples. This credit is available to any qualified workers, regardless of whether they participate in a Traditional or Roth IRA.

Explanation of Local Expenditures:

Explanation of Local Revenues: Because the bill will likely reduce state taxable income as individuals contribute to their accounts, counties imposing a local option income tax (LOIT) could experience a decrease in LOIT collections. The impact on LOIT revenue is indeterminable.

State Agencies Affected: Treasurer of State, Office of Management and Budget, Auditor of State, Department of Labor.

Local Agencies Affected:

Information Sources: IRS webpage on Traditional and Roth IRAs, http://www.irs.gov/Retirement-HERO Plans/Traditional-and-Roth-IRAs; MyRA website, https://myra.treasury.gov/;
U.S. Census Bureau, *2013 American Community Survey, Indiana: DP03 Selected Economic Characteristics;* Bureau of Labor Statistics, *National Compensation Survey-Benefits - Civilian Workers: Access to Retirement Benefits,* March 2014; http://www.bls.gov/news.release/ebs2.t01.htm; Federal Reserve Board, *2013 Survey of Consumer Finances,* http://www.federalreserve.gov/pubs/bulletin/2014/pdf/scf14.pdf.;Wolters Kluwer CCH, *2015 U.S. Master Tax Guide*, November 2014.

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